

Internal Revenue Service

Department of the Treasury

District  
Director

P.O. Box 2508  
Cincinnati, OH 45201

Person to Contact:

Telephone Number:

Refer Reply to:

EP/EO

Date: JAN 27 1989

Dear Sir or Madam:

We have considered your application for recognition of exemption from Federal income tax under the provisions of section 501(c)(7) and section 501(c)(10) of the Internal Revenue Code of 1986 and its applicable Income Tax Regulations. Based on the available information, we have determined that you do not qualify for the reasons set forth on Enclosure I.

Consideration was given to whether you qualify for exemption under other subsections of section 501(c) of the Code and we have concluded that you do not.

As your organization has not established exemption from Federal income tax, it will be necessary for you to file an annual income tax return on Form 1120 since you are a corporation.

You have agreed to the denial of exemption by executing Form 6018, Consent to Proposed Adverse Action.

Sincerely yours,

District Director

Enclosure

[REDACTED]  
(Hereinafter referred to as the Corporation)

#### Facts

The Corporation was incorporated on [REDACTED] for the following purposes:

To acquire land by purchase, lease or otherwise, and to hold and operate a park on the said land for the benefit of members of [REDACTED] and their families; and for that purpose to erect and maintain structures, lay out and maintain recreational grounds and facilities; to rent the said park to acquire funds for its operation; to sell food and non-alcoholic beverages; to sell or rent recreational equipment; and generally to do all lawful things incident to and proper to the acquisition, maintenance and operation of a recreation park.

The park is open at all times to [REDACTED] and their families free of charge. It is open at all times to non-[REDACTED] (groups such as family reunions, company picnics) on a charge or rental reservation basis. The application originally indicated [REDACTED] % of the Corporation's receipts are from nonmembers and this was latter revised to be about [REDACTED] %.

The Corporation is controlled by the [REDACTED] that own the park. Its income will come from park rental, sale of natural gas, and vending machines. If these sources are insufficient to pay the cost of the park's upkeep, the owners will provide any additional support required.

The Corporation is simply an entity organized and operated to manage a park, and is not itself a fraternal society, but a management corporation created by [REDACTED] to manage a park that they jointly own.

#### Law

##### Section 501(c)(7)

Section 501(c)(7) of the Code provides for the exemption from Federal income tax of clubs organized for pleasure, recreation, and other nonprofitable purposes, substantially all of the activities of which are for such purposes and no part of the net earnings of which inures to the benefit of any private shareholder.

Section 1.501(c)(7)-1(a) of the Regulations states that the exemption provided by section 501(a) of the Code for an organization described in section 501(c)(7) of the Code applies only to clubs which are organized and operated exclusively for pleasure, recreatic and other

nonprofitable purposes, but does not apply to any club if any part of its net earnings inure to the benefit of any private shareholder. In general, this exemption extends to social and recreation clubs which are supported solely by membership fees, dues and assessments. However, a club otherwise entitled to exemption will not be disqualified because it raises revenue from members through the use of club facilities or in connection with club activities.

Section 1.501(c)(7)-1(b) of the Regulations states that a club which engages in business, such as making its social and recreational facilities available to the general public or by selling real estate, timber, or other products, is not organized and operated exclusively for pleasure, recreation and other nonprofitable purposes, and is not exempt under section 501(a) of the Code. Solicitation by advertisement or otherwise for public patronage of its facilities is prima facie evidence that the club is engaging in business and is not being operated exclusively for pleasure, recreation, or social purposes. However, an incidental sale of property will not deprive a club of its exemption.

As previously noted, section 501(c)(7) of the Code requires that substantially all of a social club's activities be social or recreational activities for members. However, Public Law 94-568, 1976-2 C.B. 596, provides that a social club may receive up to 35 percent of its gross receipts, including investment income from sources outside its membership without losing exemption. Within this 35 percent amount, not more than 15 percent of the gross receipts should be derived from the use of a social club's facilities or services by the general public. This means that an exempt social club may receive up to 35 percent of its gross receipts from a combination of investment income and receipts from nonmembers so long as the latter do not represent more than 15 percent of the total receipts.

#### Section 501(c)(10)

Section 501(c)(10) of the Code provides for the exemption from Federal income tax of domestic fraternal societies, orders, or associations operating under the lodge system, the net earnings of which are devoted exclusively to religious, charitable, scientific, literary, educational, and fraternal purposes and which do not provide for the payment of life, sick, accident, or other benefits.

Section 1.501(c)(10)-1 of the Income Tax Regulations provides that an organization will qualify for exemption under section 501(c)(10) if it is a domestic fraternal beneficiary society, order, or association, described in section 501(c)(8) and the regulations thereunder, except that it does not provide for the payment of life, sick, accident, or other benefits to its members and devotes its net earnings exclusively to religious, charitable, scientific, literary, educational, and fraternal purposes.

Section 1.501(c)(8)-1 of the regulations provides that a fraternal beneficiary society is exempt from tax only if operated under the "lodge system" or for the exclusive benefit of the members so operating. "Operating under the lodge system" means carrying on its activities under a form of organization that comprises local branches, chartered by a parent organization and largely self-governing, called lodges, chapters, or the like.

Revenue Ruling 73-370 concerns a fraternal beneficiary society; subordinate organization formed by local lodge. A nonprofit, subordinate organization, formed and chartered by a local lodge of a fraternal beneficiary society exempt from tax under section 501(c)(10) of the Code to carry on the fraternal and charitable activities of the society in a particular geographical area, is also exempt under section 501(c)(10).

#### Conclusion

By earning 98% of its income from nonmembers, the Corporation violates the provisions of Public Law 94-568, cited above. Because the Corporation receives the majority of its income from dealings with nonmembers, it is not described in Section 501(c)(7) of the Code. Unlike the organization described in Revenue Ruling 73-370, cited above, the Corporation is not a fraternal society operating under the lodge system. It is, instead, a management corporation organized and operated to manage a park. Because the Corporation is formed to manage a park rather than operate as a fraternal society, it is not described in Section 501(c)(10) of the Code. Therefore, the Corporation is denied exemption from Federal income tax.